UNITED STATES OF AMERICA
FEDERAL MARITIME COMMISSION

Advance Notice of Proposed Rulemaking Concerning Section 6(g) of the Shipping Act of 1984	Docket No. 93-23

COMMENTS OF THE UNITED STATES DEPARTMENT OF JUSTICE

On November 29, 1993, the Federal Maritime Commission (FMC or Commission) issued an Advance Notice of Proposed Rulemaking Concerning Section 6(g) of the Shipping Act of 1984.1/ The Advance Notice sought comments on whether published guidelines for implementation of Section 6(g)2/ would be useful and appropriate to meet its enforcement responsibilities under this Section.

1/ Docket No. 93-23 (Advance Notice).

2/ 46 U.S.C. app. 1705(g):

> Substantially Anticompetitive Agreements -- If, at any time after the filing or effective date of an agreement, the Commission determines that the agreement is likely, by a reduction in competition, to produce an unreasonable reduction in transportation service or an unreasonable increase in transportation cost, it may, after notice to the person filing the agreement, seek appropriate injunctive relief under subsection (h).

SUMMARY OF POSITION

The United States Department of Justice (Department) urges the FMC to adopt guidelines patterned after the antitrust enforcement agencies' Merger Guidelines.3/ The Merger Guidelines would be useful and appropriate for the Commission because they were designed for the same task outlined in Section 6(g): assessing the likely competitive effects of changes in market structure, such as creation and operation of conferences or other joint ventures among competitors.

The Congress, courts and antitrust enforcement agencies have developed an analytical framework for defining relevant markets in order to determine whether mergers or other changes in market structure proposed by horizontal competitors are likely to reduce competition to an extent that harms the public by unreasonably raising prices or reducing output. Accordingly, the antitrust analysis reflected in the Merger Guidelines is uniquely well-suited to enable the Commission to discharge its statutory obligation of monitoring conference agreements and other agreements among ocean carriers.

The Commission's Advance Notice, however, reveals a number of incorrect assumptions about the antitrust laws and antitrust analysis. As a result, the Commission may have inadvertantly

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3/ Horizontal Merger Guidelines, issued by the U.S. Department of Justice and the Federal Trade Commission, April 2, 1992; _reprinted in_ Areeda & Hovenkamp, Antitrust Law, 1993 Supplement, Appendix A.

rejected the most useful tools available to implement its authority under Section 6(g) to identify and enjoin unreasonably anticompetitive agreements.

Discussion

I. The Standard for Section 6(g) is Consistent With Antitrust Standards as Presented in Case Law and the Merger Guidelines

A. The Antitrust Laws and Section 6(g) Have the Same Enforcement Objectives

The FMC has the responsibility to review all conference agreements prior to their implementation and to seek to enjoin any agreements that are substantially anticompetitive. Congress placed the responsibility for protecting the consuming public in the hands of the expert agency, the FMC, and as a consequence generally removed ocean carrier agreements from separate review by the federal courts under the antitrust laws.4/ Far from requiring a retreat from a vigorous antitrust standard of legality for carrier agreements, however, Section 6(g) invites the Commission to review agreements for consistency with the welfare of shippers and consumers and to seek to enjoin agreements that would not pass muster under a rule of reason standard under the antitrust laws.

The statutory goals and standards in Section 6(g) parallel closely those under Section 1 of the Sherman Act and Section 7

4/ H.R. Rep. No. 600, 98th Cong., 2d Sess. 34 (1984) ("Conference Report") at 31.

of the Clayton Act, the antitrust statutes that deal with agreements among competitors.5/ Congress expressly gave the Commission authority in Section 6(g) to protect the public from agreements that will result in an unreasonable increase in price or reduction in service. This charge parallels the goal of the antitrust laws: to protect the public from a reduction in competition caused by agreements that unreasonably increase market power, that is, the power to increase price or reduce output. Furthermore, the standards set forth for meeting these goals in the Shipping Act are similar to those in the antitrust statutes.

Section 6(g) allows the Commission to take action when it determines that the agreement is "likely" to have adverse effects on competition. Similarly, the Clayton Act prohibits any merger the effect of which "may be substantially to lessen competition" in a market, and the Merger Guidelines state that the enforcement agencies will take action when, as under section 6(g), such a reduction is "likely." Merger Guidelines at 0.1. Furthermore, Section 6(g)'s emphasis on "unreasonable" effects on transportation echoes the rule of reason antitrust analysis developed by the courts under Section 1 of the Sherman Act. Sherman Section 1 prohibits contracts and other agreements "in restraint of trade;" however, Courts recognized

5/ 15 U.S.C. § 1, 18.

quickly that any contract restrains trade to some degree and interpreted Section 1 to prohibit only those agreements that unreasonably restrain trade.6/ Courts determine reasonableness of an agreement by balancing its procompetitive benefits against its anticompetitive effects.7/ The similarity between Section 6(g) and the antitrust rule of reason was noted by the Advisory Commission on Conferences in Ocean Shipping in its April 1992 Report (Advisory Commission Report) at 82.

Because these antitrust statutory goals closely correspond to those under Section 6(g) of the Shipping Act, the Commission should turn with confidence to antitrust analysis and precedents in administering Section 6(g). Specifically, the Department suggests that in order to gauge the effect on competition of conferences and other intercarrier agreements, the Commission apply the same analysis presented in the Merger

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6/ Chicago Board of Trade v. United States, 246 U.S. 231, 238 (1918). See also Continental TV Inc. v. GTE Sylvania Inc., 433 U.S. 36, 49 (1977) (Under the rule of reason "the factfinder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited as imposing an unreasonable restraint on competition.")

7/ See, e.g., Broadcast Music, Inc. v. Columbia Broadcasting Systems, Inc., 441 U.S. 1 (1979). As a result, even price-fixing among substantially all competitors in a market has been examined under the rule of reason when necessary to achieve some economically efficient end not otherwise attainable.

Guidelines.8/ The Merger Guidelines are, after all, an articulation of "the analytical framework the Agency applies in determining whether a merger is likely substantially to lessen competition". Merger Guidelines at 1-2. The Department of Justice also uses this framework to determine whether joint venture agreements short of outright merger among competitors will be on balance procompetitive, or serve only to reduce competition. Accordingly, the Merger Guidelines framework can be used to correctly assess the competitive effect of both conference agreements and other intercarrier agreements.

B. The Merger Guidelines Framework is Appropriate For Analyzing Competitive Effects Under Section 6(g)

The Merger Guidelines set forth the steps by which the antitrust enforcement agencies ascertain whether a challenged transaction will adversely affect competition. The types of transactions that can be examined using the Merger Guidelines include both outright mergers and joint ventures, such as conferences, among competitors;9/ the analytical method of the Merger Guidelines applies to both.

8/ This suggestion was also made by the Advisory Commission. Advisory Commission Report at 83-84.

9/ A joint venture is any cooperative business venture, short of merger or acquisition, the purpose of which is to provide a new or improved service, or an existing service more efficiently. In the ocean shipping business, common joint ventures include consortia, rationalization agreements, slot chartering agreements, joint marketing agreements, and tariff publishing services.

Under the Merger Guidelines, as a first step, a market is defined in which to measure the effect of transactions. United States v. E. I. duPont de Nemours & Co., 353 U.S. 586 (1956), Rothery Van & Storage v. Atlas Van Lines, 792 F.2d 210 (D.C. Cir. 1986). Competition can only meaningfully be examined in the context of a market; that is, a group of sellers to which a buyer can practicably turn for supply of the product (or service) under examination. The Merger Guidelines require an examination of both the product (or service) and the geographic dimension of the market in which the transaction will occur, Merger Guidelines §1.0. The Commission should likewise define product (or service) and geographic markets in conducting its 6(g) analysis. Transportation markets are generally characterized by origin and destination pairs, the geographic size of which depend on a variety of commercial characteristics. In appropriate circumstances, relevant markets might be expanded due to source or product competition.10/

10/ For example, the Interstate Commerce Commission recognizes what it terms "product" and "geographic" competition in determining the market dominance of railroads. Market Dominance Determination And Consideration of Product Competition, 365 I.C.C. 118, 128 (1981). The ICC defines these as follows: "Geographic competition is a restraint on rail pricing stemming from a shipper's or receiver's ability to get the product to which the rate applies from another source, or ship it to another destination. . . . Product competition occurs when a receiver or shipper can use a substitute(s) for the product covered by the rail rate." See also Oil Pipeline Deregulation, Report of the U.S. Department of Justice (May 1986) at 16-19; Pittman, R., Railroads and Competition: The (Footnote continued on next page.)

Once the relevant markets are defined, the competitors in those markets are identified, and market shares and market concentration are determined. Merger Guidelines Section 1.5. If the relevant market proves to be unconcentrated, the likelihood of injury to competition is low and the inquiry will end. Id. Thus, under the Merger Guidelines, a conference agreement that leaves relevant markets unconcentrated need not concern the Commission.

If the relevant market is concentrated enough to raise competitive concerns, however, the Merger Guidelines then require an assessment of whether the potential for entry by new firms or expansion by existing firms will deter or counteract anticompetitive activities even within a concentrated market (Merger Guidelines Section 3.0), as well as an examination of other factors that may indicate that market concentration or share is not representative of market power. See, e.g., United States v. General Dynamics, 415 U.S. 486 (1974).

Finally, under the Merger Guidelines, any efficiency effects are to be weighed against the adverse competitive impacts. Merger Guidelines 4.0. Possible benefits include

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Santa Fe/Southern Pacific Merger Proposal, 34 J. Ind. Econ. 25 (1990); Eaton and Center, A Tale of Two Markets: The ICC's Use of Product and Geographic Competition in the Assessment of Rail Market Dominance, 53 Trans. Pract. J. 16 (1985).

facilitating entry into new markets or services that neither party is likely to provide alone. The kinds of efficiencies set forth in the Merger Guidelines include achieving scale (or scope) economies, better integration of production facilities, and combining selling, servicing and distribution functions. An example of a joint venture that would be least likely to raise competitive concern would be a joint venture between smaller carriers where they jointly manage their assets, rationalize their sailing schedules, and thereby create a larger, more efficient network.

The multistep analysis of the Merger Guidelines demonstrates that, contrary to the statement in the preamble of the Advance Notice, antitrust analysis does not posit that market concentration is determinative of market power. Assessment of market concentration is a tool, and an important tool, but not the end of the antitrust analysis. Merger Guidelines at 0.2. Congress's admonition to the Commission to look at the context of the conference agreement and not just the concentration in the market is consistent with standard antitrust analysis.11/

11/ See Conference Report at 34-35. Antitrust courts have found some types of agreements between competitors so likely to cause anticompetitive consequences unbalanced by beneficial effects that a prolonged trial under a rule of reason analysis is not necessary. Northern Pacific Railway Co. v. United States, 356 U.S. 1, 5 (1958). The *per se* rule, which is a rule designed to avoid needless litigation over an agreement's actual effects, has been limited to areas of unambiguous social loss. Under the antitrust laws, for example, a conference that (Footnote continued on next page.)

Moreover, while the Merger Guidelines framework for analysis is equally applicable, the standards for a legal challenge of a joint venture may be considerably more permissive in instances where joint ventures are of more limited scope than a full-fledged merger, such as where the partners retain their independent management and set prices and capacity independently. Many slot charter agreements fit this description and do not raise significant competitive concerns.

The Advance Notice emphasizes that the Shipping Act of 1984 required a significant departure from the method that the Commission had previously used to examine conference agreements' effect on competition. This change, while significant, was less a change of standard than one of process. Congress was concerned with the time consumed by the Commission's competitive analysis and with the burden that had been placed upon the proponents of the agreement under the Shipping Act of 1916 to prove that the agreement was in the public interest. Advance Notice at 5.

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did nothing more than fix shipping rates among its competing members would be condemned as _per se_ illegal, without showing that the conference possessed market power. While Congress rejected the use of a _per se_ test for conference agreements, that does _not_ imply a rejection of antitrust principles or analysis to weigh the reasonableness of the effect of intercarrier agreements on prices and output. It simply means that evidence on the relevant markets and likely effects of an agreement must be adduced in each case.

The remedy Congress adopted to address these procedural problems was not an abandonment of antitrust principles but a requirement of expedition and a shift of the burden of proof to the Commission to demonstrate likely anticompetitive effects. In so doing, Congress brought competition rules and procedures for ocean shipping into line with antitrust law--firms in other industries have never been required to prove their mergers or joint ventures were pro-competitive or otherwise in the public interest before they could proceed; rather the burden has always been on the government to prove the unreasonable harm to competition.

These changes also brought the Shipping Act pre-filing procedures into line with the antitrust enforcement agencies "file-and-wait" procedures. Under the Hart-Scott-Rodino premerger notification program,12/ the enforcement agencies have a limited time to review the effect of a proposed transaction on competition and the agency bears the burden of demonstrating that the transaction should not go forward. Thus, while the Shipping Act did change the procedure for examining competitive effects of conference agreements, the change brought the analysis closer to that of the antitrust agencies, not farther away.

12/ 15 U.S.C. 18(a).

For these reasons, the Commission in developing guidelines for it's own competition analysis, should take advantage of the years of development of antitrust law and principles by the courts, Congress and enforcement agencies and adopt guidelines patterned after the analysis of the Merger Guidelines.

II. Reliance on False Premises Will Result in Guidelines That are Inconsistent With the Commission's Section 6(g) Responsibilities

The Department is particularly concerned that the Commission's hesitation in incorporating antitrust precedent and economics could impair its ability effectively to monitor the competitive effects of conference agreements. The preamble to the Advance Notice reflects three misapprehensions that may limit the effectiveness of the Commission's Section 6(g) program.

First, market concentration must be considered an important, albeit not determinative, factor in competitive analysis. If the Commission ignores market concentration in its analysis, it will severely limit the effectiveness of its competitive review. Antitrust enforcement agencies gauge concentration in order to determine whether anticompetitive coordination among competitors to raise price or decrease output will be successful. As is discussed in the Merger

Guidelines at Section 2.0, "All other things being equal, market concentration affects the likelihood that one firm or a small group of firms could successfully exercise market power." If examination of the properly defined relevant market shows that it is unconcentrated, the likelihood of successful anticompetitive behavior is low. A finding of low concentration can end an inquiry and speed a final determination. Conversely, the more concentrated a relevant market, the greater the chance that the few firms in that market will be able to overcome the difficulties and costs of reaching and enforcing an anticompetitive agreement. Merger Guidelines at 2.1.13/

13/ Contrary to the assumption in the Advance Notice at 8, the legal right of conference members to engage in independent action does not limit the importance of concentration in the analysis. Members of any illegal price-fixing cartel in an unregulated industry are always able to cheat on the cartel by independently offering secret discounts--a "right of independent action" is the rule, not the exception. Cartel members have an incentive to cheat on the cartel by, for example, offering a price lower than the cartel price to some customers and increasing sales volumes. If everyone did this, of course, the cartel would collapse and no one would get the benefit of the supracompetitive prices. For this reason, discounting off of the cartel price (that is, independent action) is more likely to occur if it can remain secret. Such secret discounts are expressly prohibited under the Shipping Act. If _secret_ discounts by cartel members do not render market concentration unimportant, then the limitation that conference independent action discounts must be publicly tariffed makes concentration more important than in other industries, not less. The lack of secrecy in ocean shipping makes it less likely that discounts will be offered. Thus, concentration remains important notwithstanding a statutory right of independent action.

The Advance Notice also appears to incorrectly assume that benefits to carriers, and larger short-term profits, for example, are necessarily social benefits that can be used to counterbalance harm to competition and in discussing the potential benefits that might justify otherwise anticompetitive conference agreements, the Advance Notice appears to accept in all circumstances "overcapacity" and "rate instability" as market failures that are easily and best corrected by forming conferences or permitting other intercarrier agreements.

Yet fluctuations in rates can be useful and efficient. Price changes allow overcapacity to be reduced and scarce or constrained capacity to be allocated on a timely basis. The Advance Notice offers no explanation of why artificial rate stability as such would constitute a procompetitive benefit that could outweigh any anticompetitive element of a conference agreement, and none is apparent. If proposing to strike such a balance, the Commission's guidelines should articulate the nature of any expected procompetitive benefit to be gained by rate stability, and how such stability is expected to outweigh the anticompetitive features of the agreement.

Further, it is not clear that anticompetitive agreements are the best mechanism for dealing with rate instability. Many unregulated industries are faced with uncertain conditions that lead to unstable prices. Buyers and sellers have developed methods to control price fluctuations, including futures markets which allow parties to trade away the risk, technological innovations aimed at reducing the fluctuations in prices, and contracts that allocate the risk to the party able to handle the risk at the lowest cost. Using these mechanisms, the market has proven to be extremely effective at reducing the costs associated with price instability. In contrast, anticompetitive conference agreements, while ostensibly aimed at reducing price instability, may exacerbate the problem by impeding a market response. The same is even more likely to be true of conference agreements to control overcapacity. To the extent a conference has market power and artificially raises rates, additional capacity will be attracted to the market.

Finally, the Advance Notice appears to support a standard that would all but eliminate the possibility of pre-implementation injunction of conference agreements. Advance Notice at 13. Such a policy would eliminate one of the most important tools that the Commission has been given to allow competition to keep transportation costs low and service quality high. Because, at the preimplementation stage, "there can be no evidence of actual shipper harm" and "consequently" preimplementation review would "involve an estimate" of the economic impact and that estimate must be made "without knowledge of what rate increases the parties to the agreement intend to enact," the Advance Notice assumes that it will be unable to ascertain at that point whether an agreement is likely to cause "material" and "meaningful" harm to shippers, as is the intention of the Conferees.14/

Again, the Merger Guidelines, antitrust law and economic analysis can provide the Commission with tools for this task. It is commonplace for antitrust enforcement agencies to seek to enjoin anticompetitive transactions prior to their implementation. Prior to an actual merger or joint venture, neither the antitrust agencies nor federal district judges can measure "actual harm" in dollars or reduced output to any group of consumers, nor do they ordinarily know the exact economic impact of the agreement nor the prices that will be charged after the merger or joint venture. Yet, as discussed above, the antitrust agencies routinely ascertain the likely consequences of transactions and whether those impacts will be significant, and courts issue injunctions to prevent anticompetitive transactions. Congress not only affirmed such injunctive action by the courts on petition by the antitrust enforcement agencies, but facilitated premerger review by affording the antitrust agencies with a window of

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14/ Advance Notice at 13 quoting Conference Report at 35.

pre-implementation review for mergers that is similar to that given the Commission for review of conference agreements. The antitrust agencies' method for assessing likely competitive harm of proposed transactions is set forth in the Merger Guidelines. As such, the Merger Guidelines can provide the Commission with a mechanism for prospectively determining likely competitive effects of conference agreements.

III. Conclusion

For the foregoing reasons, the Department urges the Commission to adopt a system of guidelines modeled upon the Merger Guidelines for analysis of agreements under Section 6(g) of the Shipping Act of 1984.

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